

# BEST PRACTICES FOR WATER QUALITY TRADING

## JOINT REGIONAL AGREEMENT

### **Discussion Guide (Appendix), August 8<sup>th</sup>, 2013**

This Discussion Guide Appendix is intended to provide definitions, context, analysis, and options for addressing various components of water quality trading programs. It poses questions that will be discussed at the interagency workshops. This document may reference other trading programs, examples, or documents, but is not intended to serve as a published report or white paper and thus will not be extensively cited. This document will be included in the workshop packet and posted online following each workshop.

### **Role of State Agencies, NPDES Permittees, and Third Parties (Section 4.1,7,8)**

#### **Appendix 1: Delegation and Roles in Market Operation**

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Although water quality agencies may maintain responsibility for all aspects of a trading program, agencies may decide to delegate a number of actions to designated third parties or permittees. Delegation is most appropriate for functions where specific expertise is required, where the entity executing the function needs to be flexible (i.e., able to adjust quickly to quick shifts in demand in terms of funding and staffing), and where a high volume of transactions might cause agencies to spend time and money beyond what is available to those agency personnel. This discussion guide appendix provides examples of where agencies have decided to delegate various functions/types of responsibility to third parties. This appendix is not meant to suggest that agencies should delegate any particular functions.

Under the Clean Water Act (CWA), states have been delegated responsibility to manage the NPDES permitting program.<sup>1</sup> The CWA does not address further delegation of state authority to third parties or permittees in the trading context, and state law is similarly silent as to what aspects of managing day-to-day administration for a trading program can be delegated from a state to a private entity that would serve in a quasi-governmental role. As such, this discussion guide summarizes analogous contexts in which some aspects of a government-managed program have been delegated to third parties, and the legal contours surrounding these delegation arrangements.

#### **A. Delegation to Third Party of Monitoring/Verification/Registration, Compliance/Enforcement, and/or Standards Development**

The formality and complexity of the delegation arrangement varies depending on the types of tasks that are being delegated to a third party. Obviously, where a third party is delegated more extensive authority, there will likely be more rigid and demanding oversight requirements placed by the delegating government body. In the water quality trading context, the actions for which delegation may make sense are: A) project validation and verification; B) monitoring/inspection and maintenance; C) enforcement and compliance; and D) standards development. Following are descriptions of several delegation relationships (some examples are not as directly analogous to the water quality trading context, but provide important guiding principles for assessing delegation). These examples are organized from most extensive delegation of authority, to least extensive.

#### **I. Examples**

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<sup>1</sup> 33 U.S.C. § 1342(b).

1. **Delegation of Overall Programmatic Management Authority - Congressional Delegation of Management, Monitoring, Enforcement & Standard Development Authority to the Columbia River Gorge National Scenic Area Commission:** in 1986, Congress signed into law the Columbia River Gorge National Scenic Area Act (CRGNSAA).<sup>2</sup> The scenic area is managed on a partnership basis between the relevant Gorge counties, Oregon, Washington, the U.S. Forest Service, and the Gorge Commission. In addition the congressional authority granted in the CRGNSAA, both the Oregon and Washington legislatures signed a bi-state compact forming the agency.<sup>3</sup> The quasi-governmental Commission has authority to manage all non-federal lands within the scenic area, including through the development of land use ordinances applicable to non-federal lands within the scenic area, and through approval/denial of land use ordinances proposed by relevant counties within the scenic area.<sup>4</sup> The Secretary of the federal Agriculture Department does have final approval/disapproval of Commission-designed land use ordinances.<sup>5</sup> The Commission can monitor county activities for compliance with approved land use ordinances, issue orders to ensure compliance, or assess civil penalties.<sup>6</sup>
2. **Delegation of Overall Programmatic Management Authority – Congressional Delegation of Private Land Management Responsibilities in Congressionally-Designated Wild & Scenic River Corridor to a Local Management Council:** Congress designated a largely privately owned portion of the Niobrara River as a wild & scenic river corridor. To manage the land, Congress established an advisory committee to aid the National Park Service (NPS)—the federal land management agency responsible for managing the W&S river corridor—in developing and carrying out a land management plan for the corridor.<sup>7</sup> This advisory committee established a local council (composed of 9 local private members—4 landowners, 1 timber industry representative, 1 recreational business representative, 4 county commissioners, 2 local natural resource district representatives, 1 state representative, only 2 federal representatives) responsible for managing the land.<sup>8</sup> Ultimately, the federal courts deemed that management structure was unlawful because the NPS did not retain final power or oversight control over the decisions of the local council, and because the private members of the local council had real/potential conflicts of interest.<sup>9</sup> Moreover, the court found council did not have the authority to enforce laws in the way that the NPS would otherwise been able to do.<sup>10</sup> The court determined agency authority to cancel the delegation is not sufficient control.<sup>11</sup>
3. **Delegation of Standard Development, Compliance & Enforcement – North American Electric Reliability Corporation (NERC) Delegation to the Western Electricity Coordinating Council (WECC) to Develop Reliability Standards, and to Monitor/Enforce:** the Western Electricity Coordinating Council (WECC) is a Utah-incorporated non-profit entity responsible for coordinating and promoting bulk electric system reliability in the Western Interconnection.<sup>12</sup> With the approval of the Federal Energy Regulatory Commission (FERC) through a contractual agreement, WECC was delegated this authority by the North

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<sup>2</sup> 16 U.S.C. § 544 – 544p.

<sup>3</sup> *Id.* § 544c.

<sup>4</sup> *Id.* § 544e, f(i)(2).

<sup>5</sup> *Id.* § 544f(j).

<sup>6</sup> *Id.* § 544m.

<sup>7</sup> *Nat'l Parks Conserv. Ass'n v. Stanton*, 54 F.Supp.2d 7, 10 (D.D.C. 1999).

<sup>8</sup> *Id.* at 11.

<sup>9</sup> *Id.* at 7.

<sup>10</sup> *Id.* at 18-19.

<sup>11</sup> *Id.* at 21.

<sup>12</sup> WECC, Bylaws of the Western Electricity Coordinating Council, § 16 (2012) (appendix to delegation agreement between NERC and WECC) (hereafter “WECC Bylaws”).

American Electric Reliability Corporation (NERC)—which itself is a third party designee of the Federal Energy Regulatory Commission (FERC).<sup>13</sup> The delegation agreement is valid for a 5-year term.<sup>14</sup>

Under this arrangement, WECC has the authority to develop, and enforce reliability standards through any enforcement mechanisms delegated to it pursuant to the Federal Power Act.<sup>15</sup> These standards must be submitted to NERC for approval.<sup>16</sup> WECC also operates a compliance and enforcement program that tracks compliances with mandatory reliability standards approved by FERC and Canadian/Mexican counterpart agencies.<sup>17</sup> WECC does not have the authority to monitor or enforce compliance for itself or an affiliate.<sup>18</sup> Moreover, WECC is required to maintain a conflict of interest policy.<sup>19</sup> At least every five years, the designee (NERC) has to review WECC's compliance and enforcement program.<sup>20</sup> WECC must also report to NERC on the performance of its functions and related activities.<sup>21</sup>

Where a market issue develops, WECC can try to resolve the issue through voluntary solutions, or if necessary, propose a solution to an applicable regulatory authority (i.e., FERC, or state/provincial government agency with jurisdiction to regulate).<sup>22</sup> If mediation or arbitration does not resolve a dispute involving WECC, an appeal may be made to FERC.<sup>23</sup>

4. **Delegation of Credit Verification/Registration Authority - Western Governors' Association Delegation of Authority to the Western Renewable Energy Generation and Information System (WREGIS) to Develop and Manage Online Renewable Energy Credit Verification & Registration:** WECC also houses the Western Regional Energy Generation Information System (WREGIS), which was formed by means of a collaborative process involving the Western Governors' Association, the state of California, and the Western Regional Air Partnership.<sup>24</sup> In 2004, the Western Governors' Association amended their Energy Policy Roadmap resolution to support the creation of an independent regional tracking system to provide the data needed to substantiate and support the verification and tracking of renewable energy generation.<sup>25</sup> WREGIS tracks renewable energy generation from units that register in the system by using verifiable data and creating renewable energy certificates (REC) for this generation. One WREGIS certificate (with a unique serial number) is created for each megawatt-hour of renewable energy produced; these certificates can be used by electricity suppliers to comply with relevant state/provincial policies (e.g., renewable portfolio

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<sup>13</sup> Amended and Restated Delegation Agreement between North American Electric Reliability Corporation and Western Electricity Coordinating Council, § 4 (2011, approved by FERC March 1, 2012), *available at* <http://www.wecc.biz/library/WECC%20Documents/Business%20and%20Governance%20Documents/Delegation%20Agreement%20-%20Version%207.pdf> (hereafter "NERC-WECC Delegation Agreement").

<sup>14</sup> NERC-WECC Delegation Agreement, § 12(b).

<sup>15</sup> WECC Bylaws, §§ 2.1.4, 2.1.7 (2012) (appendix to delegation agreement between NERC and WECC).

<sup>16</sup> NERC-WECC Delegation Agreement, § 5.

<sup>17</sup> *Id.* § 4.8. WECC can also suspend or terminate a WECC member.

<sup>18</sup> *Id.* § 4(a).

<sup>19</sup> *Id.* § 6(h).

<sup>20</sup> *Id.* § 6(i).

<sup>21</sup> *Id.* § 8(a).

<sup>22</sup> WECC Bylaws, § 2.1.10.2 (the definition of regulatory authority appears in section 3.3 of the WECC Bylaws).

<sup>23</sup> *Id.* § App. C, § C.10.

<sup>24</sup> WREGIS, Operating Rules § 1 (2013), *available at*

<http://www.wecc.biz/WREGIS/Documents/WREGIS%20Operating%20Rules.pdf>.

<sup>25</sup> Letter from Pam Inmann, Exec. Director of Western Governors' Ass'n, to Ronald Nunnally, Chairman of the Western Electricity Coordinating Council (July 19, 2004), *available at*

[http://www.wecc.biz/committees/BOD/072904/Lists/Agendas/1/0704\\_WREGIS\\_Agenda\\_Item\\_VII.pdf](http://www.wecc.biz/committees/BOD/072904/Lists/Agendas/1/0704_WREGIS_Agenda_Item_VII.pdf) (referencing revised resolution).

standards) and to support voluntary green electricity markets.<sup>26</sup> WREGIS performs the measurement and verification underlying REC issuance.<sup>27</sup> Any dispute between WREGIS and a credit account holder than cannot be resolved between the party and WREGIS is subject to binding arbitration.<sup>28</sup>

5. **Delegation of Responsibility to Design and Implement Pilot Projects, Including Responsibility to Develop Standards, Monitor, and Verify** – Indiana, Kentucky and Ohio, and Ohio River Valley Water Sanitation Commission (ORSANCO) Delegation of Authority to the Electric Power Research Institute (EPRI): EPRI proposed to improve water quality in the Ohio River Basin through the development and implementation of an interstate water quality trading program.<sup>29</sup> EPRI received authority to develop and implement the pilot program through three primary mechanisms. First, ORSANCO—which was formed as the result of a multi-state compact—passed a resolution supporting the development of the program.<sup>30</sup> Second, EPRI received endorsements from EPA and USDA in the form of support letters.<sup>31</sup> And third, the states of Indiana, Kentucky, and Ohio signed an informal agreement that (a) acknowledged EPA/USDA support for the project; (b) authorized and endorsed EPRI’s proposed project plan; and (c) expressed agreement to work collaboratively toward pilot project implementation.<sup>32</sup> Under the authority delegated to it by the agreement, EPRI designed a protocol for establishing, validating, and verifying credits.<sup>33</sup> EPRI can also select and approve projects based on the applications/ rankings provided by the participating state agencies.<sup>34</sup> During the pilot program, the state agencies will periodically monitor projects and submit verification projects to EPRI.<sup>35</sup> The state agencies retain the authority to certify a credit after verification.<sup>36</sup>
6. **Delegation of Monitoring/Inspection Authority** – Oregon DEQ delegation of On-Site Wastewater Treatment System Monitoring & Inspection Authority to Certified Maintenance Providers: Oregon DEQ regulations allow an appropriately certified third party to inspect and maintain installed systems. A third party “maintenance provider” performs maintenance of on-site wastewater treatment systems. This provider must possess adequate skills and knowledge to “competently inspect and maintain” these systems, and must be appropriately certified and have appropriate training from the manufacturer.<sup>37</sup> DEQ may enter into inter-agency agreements to train and certify maintenance providers.<sup>38</sup> Maintenance provider training must include at least 8 hours of hands-on training regarding relevant topics, and the

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<sup>26</sup> WREGIS, Operating Rules § 1.

<sup>27</sup> *Id.* § 9.8.3.

<sup>28</sup> *Id.* § 3; WREGIS, Account Holder Registration Agreement, § 24 (2012), *available at* <http://www.wecc.biz/WREGIS/Documents/WREGIS%20Terms%20of%20Use.pdf>.

<sup>29</sup> Electric Power Research Institute, Pilot Trading Plan 1.0 for the Ohio River Basin Interstate Water Quality Trading Project (2012), *available at* <http://www.farmland.org/documents/ORBTradingPlan8-6-12V2FINAL.pdf>.

<sup>30</sup> *Id.* at App. F (citing Ohio River Valley Water Sanitation Commission, Resolution 2-11, Development of an Interstate Water Quality Trading Program for the Ohio River Basin (2011)).

<sup>31</sup> *Id.* at App. F (Letter from Bob Perciasepe, Deputy Admin. Of Water Quality for EPA, to Alan Viceroy, Exec. Director of ORSANCO (2011); Letter from Harris Sherman, Under Secretary for USDA, to Jessica Fox, Electric Power Research Institute (2012); Letter from James D. Giattina, Director, Water Protection Division, EPA to Jessica Fox, Electric Power Research Institute (2012)).

<sup>32</sup> *Id.* at 10.

<sup>33</sup> *Id.* at App. E.

<sup>34</sup> *Id.* at E-6.

<sup>35</sup> *Id.* at E-7.

<sup>36</sup> *Id.* at E-8.

<sup>37</sup> Or. Admin. R. § 340-071-0100(95)(a)-(b).

<sup>38</sup> *Id.* § 340-071-0650.

prospective maintenance provider must pass a proficiency exam in order to become a verified provider.<sup>39</sup> This certificate can be suspended or revoked.<sup>40</sup>

7. **Delegation of Standard Development Authority** - EPA delegation to ASTM of “All Appropriate Inquiry” Standard Development for Hazardous Waste Pre-Purchase Assessment Requirements: In order to qualify for a CERCLA “innocent landowner” defense, a purchaser of property later found to be contaminated with hazardous waste materials must show that it conducted “all appropriate inquiry” prior to purchasing the site.<sup>41</sup> In essence, what constitutes an appropriate inquiry depends on what the commercial standard was at the time of purchase. EPA provides a comprehensive regulation detailing the contours of an appropriate inquiry,<sup>42</sup> but it also states that conformance with privately-developed industry standards from the American Society for Testing and Materials (ASTM) is sufficient to establish the defense.<sup>43</sup> This regulatory mechanism provides flexibility as standards evolve, and affords a third party the responsibility to modify standards.
8. **Delegation of Registration/Tracking System Authority** – Local Government Delegation of Authority to Online RME to manage Online Septic System Installation and Inspection Reporting System: several local government entities in the Northwest have contracted with Online RME for compliance reporting databases.<sup>44</sup> Third party inspectors of onsite wastewater treatments systems enter information into the website. The third party entity (Online RME) is responsible for managing the database; the overseeing government agency retains access to the information. Ostensibly, this relationship is not formally delegated, but is a contract service solicited through a request for proposal (RFP) process from a local government that Online RME bid for and won.

**II. Recommended default:** There is no recommended default. However, where delegation of tasks in a water quality trading is considered as a formal matter (such that these aspects of trading can be required in permits and other enforceable documents), the following elements should be considered and accounted for, depending on the nature of responsibility being afforded to the designee:

- *The More Extensive the Delegated Responsibilities, the More Formal/Extensive the Delegation Action Must be:*
  - *Some Official Delegation Mechanism:* delegation can occur through a semi-formal, or formal process, depending on the responsibilities being delegated. Legislative bodies can provide this formality through an appropriate legislative action. This type of action usually results in more extensive delegated authority in the designee (i.e., Congress or a state legislature provides statutory delegation authority through bicameral act or interstate compact). Executive agencies can provide this formality through a written agreement with a finite expiration/review date. This

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<sup>39</sup> *Id.* § 340-071-0650(3)(d).

<sup>40</sup> *Id.* § 340-071-0650(3)(d)(6).

<sup>41</sup> 42 U.S.C. §§ 9601(35)(B)(i)(I); 9607(b)(3).

<sup>42</sup> 40 C.F.R. pt. 312.

<sup>43</sup> 40 C.F.R. § 312.11(a) (“The following industry standards may be used to comply with the requirements set forth in §§ 312.23 through 312.31: (a) The procedures of ASTM International Standard E1527-05 entitled “Standard Practice for Environmental Site Assessments: Phase I Environmental Site Assessment Process.”).

<sup>44</sup> For example, Kitsap and Clark Counties in Washington State all use Online RME to manage tank inspection monitoring reports. See, e.g., Kitsap County Board of Health Ordinance 2008A-01 (2012), *available at* <http://www.kitsappublichealth.org/environment/files/policies/15a.pdf>; Clark County Public Health, View Your Septic System Information Online, <http://www.clark.wa.gov/public-health/septic/maps.html>.

type of delegation action is appropriate where an entity is going to undertake a large slate of responsibilities (e.g., NERC-WECC agreement). Executive agencies can also delegate authority through administrative rule (e.g., Oregon maintenance provider rules, or the federal regulations for ASTM-defined “all appropriate inquiry”) or resolutions (e.g., ORSANCO resolution supporting the development of EPRI’s trading program). Less formal delegation mechanisms—such as through a resolution from a quasi-governmental entity (e.g., resolution from the Western Governors’ Association to vest WREGI with the authority to manage REC verification, certification and registration), or through a RFP contracting process (e.g., management of online septic tank inspection/reporting system)—may also suffice if the powers being delegated are less extensive.

- *Retention of Standard Approval Authority by Overseeing Government Agency:* If authority to develop standards is delegated to a third party, the delegating government agency should retain oversight and final decision-making/approval authority over final standard approval/release and significant amendments to the standard thereafter. Significant amendments include changes in trading ratio, types of trades or trading metrics (e.g., addition new BMPs or quantification methods), or changes to trading parameters (e.g., addition of a pollutant eligible to trade). The delegating government agency would not require approval for minor amendments to the program, provided they are consistent with the overall direction and objectives. Specific to standard development, the delegating government body should provide a process for approving/modifying those standards.
- *Retention of Dispute Resolution Authority:* The applicable government agency should retain dispute resolution authority if disputes arise between the designee of delegated authority, and an entity interacting with that designee (especially if the designee has been delegated authority to oversee compliance/enforcement actions), or require binding arbitration if voluntary dispute resolution tactics are unsuccessful. In the water quality trading context, such a dispute could arise between a third party site verifier and a project developer as to the number of credits generated from a site. In order to resolve that dispute, the designee or the project developer should be able to seek review and a binding decision from the delegating agency.
- *If Designee Plans to Apply Standards to Other Third Parties, Verifiers/Inspectors Need to be Properly Trained & Accredited:* The relevant agency should require minimum proficiency (as established through an accreditation exam). Accreditation should be subject to suspension or revocation. The training program may be administered or approved by the relevant agency.
- *Avoid Conflicts of Interest for Designee or Agents of Designee:* the third party designee should avoid conflicts of interest. Such conflicts would arise if the delegated party has a financial stake in the area for which it has been delegated, or if it is privy to confidential information. Such an example might arise if a project verifier also works for a project developer, or if a standard developer is also involved in building projects.

### **III. Reasons to deviate from the default: N/A**